

HMRC internal manual

Cryptoassets Manual

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(/hmrc-internal-manuals/cryptoassets-manual/updates)

CRYPTO61212 - Decentralised Finance: Lending and staking: Income tax: Making a DeFi loan: Taxing Provisions

HMRC does not consider the return (see CRYPTO61130 (<https://www.gov.uk/hmrc-internal-manuals/cryptoassets-manual/crypto61130>)) earned by the lender/liquidity provider to be interest for tax purposes (see CRYPTO61110 (<https://www.gov.uk/hmrc-internal-manuals/cryptoassets-manual/crypto61110>)). Consequently, any provisions in the Taxes Acts which apply to interest specifically will not apply to the return. How the return is taxed will depend on whether the receipt has the nature of capital or revenue. For guidance on determining the nature of the return, see CRYPTO61214 (<https://www.gov.uk/hmrc-internal-manuals/cryptoassets-manual/crypto61214>).

Capital Receipt

If the return has the nature of capital, then the return will not be chargeable to Income Tax and will instead be within the scope of Capital Gains Tax (see CRYPTO61630 (<https://www.gov.uk/hmrc-internal-manuals/cryptoassets-manual/crypto61630>)).

Revenue Receipt

If the return has the nature of income, then it will be within the scope of Income Tax. On the assumption that the transactions are not part of a trade carried on by the customer, the receipt will be within the scope of the miscellaneous income provisions (Part 5 ITTOIA 2005).

Sections 687-689 ITTOIA 2005 (known as the “sweep-up provisions”) charge to Income Tax income from any source that is not otherwise charged under or as a result of any other provision of ITTOIA 2005 or any other act. For guidance on the miscellaneous income sweep-up provisions generally, please see BIM100000 (<https://www.gov.uk/hmrc-internal-manuals/business-income-manual/bim100000>).

Numerous cases have considered the scope of the miscellaneous income sweep-up provisions. Broadly, the result is that the reward will be chargeable under the miscellaneous income sweep-up provisions if it has the character of income and results from an understanding between both parties that the recipient will remunerate the provider for their services, for example, if there is a quid pro quo. It does not matter that a formal written contract does not exist. For further guidance on the relevance of contracts and arrangements, please see BIM100105 (<https://www.gov.uk/hmrc-internal-manuals/business-income-manual/bim100105>).

When a lender/liquidity provider lends/stakes tokens to a borrower/decentralised finance (DeFi) lending platform, there will be an agreement between the borrower/DeFi lending platform and the lender/liquidity provider. This agreement, which may fall short of being considered an enforceable contract, will set out the terms of the loan/staking, including:

- the borrowing term which may be fixed or indefinite
- the principal of the loan/staking
- any return payable by the borrower/DeFi lending platform to the lender/liquidity provider

It does not matter if the amount to be paid is unknown (for example, if the rate of return fluctuates or the borrowing period is indefinite), only that there exists an obligation on the borrower/DeFi lending platform to pay. As a result, if the return has the nature of income the return will be chargeable to Income Tax under the miscellaneous income sweep-up provisions (sections 687-698 ITTOIA 2005).

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